

## **Section 108 Loan Guarantees**

Financing for large scale, revenue producing economic development, housing, and public facilities development activities.

### **Program Description**

Section 108 Loan Guarantees assist revenue producing development activities. The program provides access to federal loans or guarantees for gap financing within small cities and towns in Massachusetts. Section 108 may assist projects undertaken by the municipality (infrastructure, housing) or by a business (economic development, housing). As with EDF community grants, assistance to non-profit organizations for public services, capitalization of loan funds or business technical assistance, or direct assistance to individual businesses or other entities for purchase of machinery and capital equipment, working capital and credit refinancing will also not be considered in Section 108.

Section 108 loan funding is provided through the sale of bonds by the U.S. Department of Housing and Urban Development (HUD) to private investors. To protect the bondholders' investment, the Commonwealth pledges to HUD a portion of its annual Community Development Block Grant (CDBG) as a guaranteed source of loan repayment. Depending on the nature of the project, HUD may also require additional security/collateral from local non-CDBG sources, up to and including a pledge of full faith and credit.

For each project, the community and/or the private sector or non-profit entity must already have secured substantial private financing support that is firm and documented. Projects which are speculative in nature or financially risky are not eligible.

### **Eligible Applicants**

Non-entitlement communities (under 50,000 population; no direct relationship with HUD for CDBG funding) in Massachusetts. Communities apply either on their own behalf or on behalf of a specific private sector borrower. The project must meet Sustainable Development Principles to be eligible to apply.

### **Eligible Activities and Funding Requirements**

Revenue producing economic development and housing projects such as:

- Economic development activities eligible under CDBG (limited to real estate, vs. user projects)
- Acquisition of real property;
- Rehabilitation of publicly owned real property;
- Housing rehabilitation eligible under CDBG;
- Construction, reconstruction, or installation of public facilities (including street, sidewalk, and other site improvements);
- Related relocation, clearance, and site improvements; and
- Payment of interest on the guaranteed loan and issuance costs of public offerings.

### **Funding Limits**

- The minimum award is \$500,000 and the maximum is \$5 million. The overall Section 108 Program is limited to \$10 million in FY 2012. The loan amount will not be included in the \$1 million annual limit that grantees may receive from the Commonwealth's annual CDBG allocation.
- Section 108 Loans generally cannot exceed 40% of the total project costs. However, DHCD will consider guaranteeing public infrastructure projects to a percentage greater than 40% on a case by case basis.
- Where job creation or retention is the national objective, a ratio of one job for every \$20,000 of Section 108 guarantee/loan assistance is used.

## Loan Details

- **Security:** The principal security for the loan guarantee is a pledge by the State of its current and future CDBG funds. Additional security will also be required to assure repayment of guaranteed obligations. The additional security requirements will be determined on a case-by-case basis, but could include assets financed by the guaranteed loan.
- **Repayment:** The maximum repayment period for a Section 108 loan is twenty years. HUD has the ability to structure the principal amortization to match the needs of the project and borrower. Each annual principal amount will have a separate interest rate associated with it.
- **Financing Source:** Section 108 obligations are financed through underwritten public offerings. Financing between public offerings is provided through an interim lending facility established by HUD.
- **Interest Rates:** Interest rates on interim borrowing are priced at the 3 month London Interbank Offered Rate (LIBOR) plus 20 basis points (0.2%). Permanent financing is pegged to yields on U.S. Treasury obligations of similar maturity to the principal amount. A small additional basis point spread, depending on maturity, will be added to the Treasury yield to determine the actual rate.
- **Default:** To date, there has been no default under Section 108 resulting in a repayment by HUD. In the event of default requiring a payment, HUD would continue to make payments on the loan in accordance with its terms. The source of payments by HUD pursuant to its guarantee would almost always be pledged CDBG funds. However, HUD does have borrowing authority with the U.S. Treasury if the pledged funds are insufficient.
- Prepayment penalties
- Guaranteed party/borrower pays legal fees

## Additional Program Requirements

- Privately owned, non-residential real estate activities where the scope exceeds exterior façade improvements consistent with EDF Program Guidance, Appendix M, must be undertaken as economic development activities and must meet CDBG underwriting criteria. These criteria limit assistance to gap financing, which may be less than the 40% program limit;
- All Section 108 applications must include evidence that the proposed project needs grant assistance to be feasible;
- DHCD is willing to consider phased projects, with the caveat that the time frame for full implementation is a maximum of five years or less;
- DHCD or HUD may disapprove applications, or approve a reduced guarantee or approve the request with conditions, such as but not limited to additional collateral and guarantees depending on the structure of the proposal; and

## Selection Criteria

The business must be located in an eligible community and the project must: meet CDBG National Objectives; show financial need/gap; provide adequate cash flow and collateral to support/repay the debt. A community must meet Sustainable Development Principles.

## How to Apply

Applicants must contact DHCD prior to submission of an application. Rolling application with two-step process: prescreening to determine if the project meets funding criteria; if so, municipality is asked to apply. Applicants provide information on both the business and the community. Project applications must

meet all applicable criteria outlined for EDF community grants. However, the format of any final loan application will be determined by HUD.

### **Application Guidelines**

- Section 108 regulations apply (24 CFR Subpart M, 570.700 - 570.710)
- Baseline employment summary, slum & blight analysis or other applicable national objective documentation will be required prior to application.
- Applicable EDF application components apply ( see EDF Application Guidance)
- Community and/or business financial information.
- Approvals may take 4- to 6-months (HUD Washington DC approval required).

### **Contact**

For additional information, please call the Division of Community Services at 617-573-1400.

### **Loan Default**

In the event of loan default, DHCD must be prepared to repay the Section 108 loans to HUD out of the Commonwealth's annual CDBG allocation. In addition to a pledge of future CDBG funds, collateral is provided from other sources, and the two noted above will be heavily collateralized with non-CDBG resources. The possibility exists, however, that the loans default and will need to be repaid from the annual allocation. In FY 2012 the potential liability, or repayment total, could be up **to** \$330,000 in the event of loan default.

If the loans do not default, or if there is default but the collateral is sufficient to cover the loan repayment (or a portion thereof), then DHCD will reallocate the budgeted default amount among other program components.

Please note that DHCD and HUD scrutinize Section 108 projects very carefully since any loan defaults are guaranteed by future CDBG funds and therefore could significantly affect availability of funds in future years.

### **Examples (Active Section 108 Loans)**

Everett – \$1 million Section 108 loan for roadwork (right-of-way & construction) for the Norman St./Internet Dr. intersection and entryway into the Rivers Edge (previously Telecom City) project area. The debt service for years 1-8 (FY 2008 – 2015) will be funded with a \$1.2 million Brownfield's Economic Development Initiative (BEDI) grant. The State CDBG Program will further guaranty this loan in years 9-20, FY 2016-2027.

North Adams - Massachusetts Museum of Contemporary Art (MASS MoCA): Approximate \$3.77 million loan to partially fund real estate development by the non-profit museum foundation. The \$13 million project involves rehabilitation of two buildings. This project is Phase II of the City and MASS MoCA's revitalization plan for one of North Adams' most distressed neighborhoods. The State CDBG Program guarantees this loan for the 20-year term FY 2004-2022.